

National Assembly for Wales Finance Committee

Call for information: Welsh Government draft budget proposals for 2018-19

Submission by the Bevan Foundation

1. Thank you for the opportunity to contribute to the Committee's consultation on the Welsh Government's draft budget. The Bevan Foundation is an independent, charitable think tank whose purpose is to make Wales fair, prosperous and sustainable by generating practical proposals. It has an extremely modest budget (£127,000 in 2016/17) does not receive any Welsh Government funding.
2. Our response covers three areas in which we have significant expertise: poverty reduction and welfare reform; Brexit and new devolved taxes.

Poverty reduction and welfare reform

3. Poverty imposes very significant costs on the Welsh budget – some £3.6 billion a year¹ - as well as affecting economic performance, social cohesion and individual lives. It makes financial sense if nothing else for the Welsh Government to seek to reduce the burden of poverty.
4. Our work with the Joseph Rowntree Foundation² has identified five key areas of intervention which are proven to reduce poverty:
 - a. **Economy:** stimulating the creation of more and better jobs especially in deprived areas.
 - b. **Education and learning:** closing the gap in attainment between poor children and others, enhancing work-related adult learning and providing personalised careers advice to all ages.
 - c. **Helping families:** with 15 hours of quality childcare for 2-5 year olds and providing parenting and additional mental health services for families.
 - d. **Cutting costs:** especially housing, energy and 'enabling' services such as public transport and internet access.
 - e. **A fair social security system:** including devolved welfare support such as the Discretionary Assistance Fund, council tax support and mitigating negative impacts of welfare reform.
5. The quantum allocated to each of these areas is clearly important – we note that several of the public services that are proven to make a difference have been subject to substantial cuts in recent years, such as part-time adult education, Careers Wales, and support for public transport.

¹ Excluding social security, lost tax revenues and other non-devolved costs (except policing and criminal justice).

² Prosperity without Poverty: a framework for action,

<https://www.bevanfoundation.org/publications/prosperity-without-poverty-framework-action-wales/>

6. However the question **how** the budget allocation is used and **who benefits** from expenditure is at least as important. The evidence rejects a model of 'trickle down' and instead suggests a 'bottom up' approach to public spending is more effective at reducing poverty. For example:
 - a. increasing expenditure on wages at the bottom of the income distribution,
 - b. increasing the attainment of children who receive free school meals
 - c. boosting skills of adults without level 3 qualifications,
 - d. reducing the costs of essential and enabling services such as housing and energy.
7. The question is therefore not just one of budget allocation but of accompanying policies and priorities. In the absence of Communities First, how public services reach and deliver to the least well-off people and places is all the more critical.

Brexit

8. The Bevan Foundation is currently working with a range of partners to develop a policy agenda for Wales after Brexit. With Brexit potentially occurring just after the end of the next budget period it is vital that the Welsh Government has contingency plans for the run-up to and immediate aftermath of Brexit, whatever form that may take, as well as longer-term plans for the future.
9. The key areas of impact are likely to be:

The economy and trade:

10. Although it is impossible to forecast the immediate as well as longer-term impact of Brexit, it is very likely to bring a period of significant economic restructuring.
11. In terms of assessment, it is unclear if the Welsh Government has identified where the risks and opportunities lie, whether this is in respect of sectors facing greatest threats or with most potential opportunities, and the risks of disruption e.g. at ports and airports. Depending on the view reached, the Welsh Government may need to or wish to change its approach to the economy and transport, e.g. providing additional support for businesses, drawing up contingency plans etc. and reducing its emphasis on inward investment.
12. There are also risks in the supply chain, with the potential of some goods and services no longer being available or substantial price rises because of tariffs or changes in the value of sterling. For example, house-builders have already identified challenges procuring some building materials. The supply of other items, including essential medicines, components and even basic foodstuffs could also be affected. We are not aware if there are risk assessments and contingency planning being undertaken in the public sector.

Movement of labour

13. The impact of Brexit on labour supply is virtually impossible to forecast because it depends not only on the agreement reached between the UK and the EU and any post-Brexit immigration regime, but only on individuals' preferences. The questions are whether the Welsh Government has identified the key risks e.g. which occupations and sectors are particularly dependent on EU workers and whether the Welsh Government is doing enough

to mitigate the risks e.g. through investment in training, proposing support for EU citizens wishing to remain, modifications to recognised qualifications.

Changes in regulation and procurement

14. Huge areas of regulation will be repatriated to the UK Government and possibly the Welsh Government. The challenges will arise if and when those regulations are changed. For example is there sufficient capacity to propose practical reforms appropriate to Wales' needs and to scrutinise legislative changes – for example what kind of post-Brexit procurement policy would work best? Is there sufficient capacity to implement changes? What might be the costs of change?

Impact on public finances

15. Most attention in Wales has been on the potential loss of European Structural and Investment funds. As we have argued in our paper prepared in partnership with the Welsh Local Government Association,³ it is vital that the UK Government's commitment to provide funding for regional development is honoured, that Wales' allocation is based on need and not the Barnett formula, and that control over how the funding is used is devolved.
16. More widely, there is huge uncertainty about the impact of Brexit on public spending. Most mainstream economists predict that UK output will shrink as a result with implications for tax revenues. How that translates into public expenditure depends on political decisions as well as the state of the economy, however it is safe to say that there are no indications that pressure on public spending will ease and some prospects that constraints could increase.
17. As well as the possibility of incurring costs associated with change, whether this is training, recruitment or increased staffing, the Welsh Government could well face a further squeeze on expenditure.

How the Welsh Government should use new taxation and borrowing powers

18. The Bevan Foundation's 2016 report 'New Taxes for a Better Wales' argued that the Welsh Government should use the powers in the Wales Act (2014) to introduce at least one new, devolved tax. In theory anything can be taxed but our proposals focused on taxes which had the potential to change behaviour (rather than simply generate revenue), were practical and had a good prospect of passing the UK Government's 'tests' for new taxes.
19. Of the eight taxes we proposed, two were introduced by the UK government as our work drew to a close (a tax on sugary drinks and the levy on apprenticeships) and three have been shortlisted by the Cabinet Secretary for Finance.
20. In respect of Land Transaction Tax, the Bevan Foundation has urged a progressive approach. For residential property transactions, we suggested that bands should be set which reflect the structure of the housing market with the transactions in the lowest bands being set to

³ After Brexit: Regional Economic Policy in Wales <https://www.bevanfoundation.org/publications/brexit-regional-economic-policy-wales/> 33

nil. We did not comment on tax on commercial transactions.

21. New devolved taxes together with the introduction of partially-devolved income tax will account for approximately 20 per cent of the Welsh Government's expenditure. This shift brings an element of risk to the Welsh Government's finances as well as requiring a new approach.

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